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CHKR - Q1 2012 Chesapeake Granite Wash Trust Earnings Conference Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

Kevin Smith *Raymond James - Analyst*

Aaron Terry *Kayne Anderson Rudnick Investment Management - Analyst*

Charles Springfield - *Private Investor*

PRESENTATION

Operator

Good day and welcome, everyone, to the 2012 Q1 Chesapeake Granite Wash Trust earnings conference call. Today's conference is being recorded. At this time I would like to turn the conference over to Nick Dell'Osso. Please go ahead, sir.

Nick Dell'Osso - Chesapeake Granite Wash Trust - EVP & CFO

Good morning, and welcome to the Chesapeake Granite Wash Trust conference call for the 2012 first quarter. Joining me for the call this morning is Steve Dixon, Executive Vice President and Chief Operating Officer of Chesapeake, and John Kilgallon, Senior Director of Investor Relations and Research.

Joining us via teleconference is Michael Ulrich, the Vice President Bank of New York Mellon Trust Company, the trustee for Chesapeake Granite Wash Trust. I have a few prepared remarks, then we will take any questions you may have.

Please note that today's call will contain forward-looking statements and assumptions that are subject to inherent risks and uncertainties. The actual results may differ materially from those projected in the forward-looking statements. Additional information about risk factors and other factors that could potentially affect the Trust and its financial results are included in the Trust's press release issued yesterday and in the Trust's filings with the SEC.

As a reminder, CHKR is a statutory trust, which is required to distribute all cash flow after expenses. The Trust has no employees or officers, and Chesapeake Energy Corporation, as a sponsor of the Trust, is responsible for the operating properties in which the Trust has an interest and fulfilling certain drilling commitments which are detailed in the Trust's prospectus.

The distribution for the three-month period ended February 29, 2012, from CHKR will be approximately \$0.66 per unit, which will be paid on May 31, 2012, to unitholders of record at the close of business on May 21, 2012. The distribution for this period is approximately 11% lower than the target distribution per unit listed in the Trust prospectus filed with the SEC on November 14, 2011. The lower distribution as compared to the original targeted amount is almost entirely driven by lower commodity prices, specifically natural gas and natural gas liquids.

For the three-month period of December through February 2012 sales volumes attributed to the Trust's royalty interest were 182,000 barrels of oil, 315,000 barrels of natural gas liquids, and 2.9 billion cubic feet of natural gas for total sales of 984,000 barrels of oil equivalent or BOEs. This compares to the projected sales volumes in the prospectus of 967,000 BOE for the same period, resulting in sales volumes net to the Trust approximately 2% higher than previously projected.

Realized prices for the period were \$97.03 per barrel of oil, \$36.56 per barrel of natural gas liquids, and \$1.90 per Mcf of natural gas. These prices include the effects of transportation and third-party deductions.



When compared to the projected prices in the November 2011 prospectus for the 2012 first quarter, unhedged realized oil prices are higher by \$7.41 per barrel. However, this is offset by unhedged, realized natural gas liquids prices, which were lower by \$6.91 per barrel, and natural gas prices, which were lower by \$0.86 per Mcf.

Turning to hedges, actual NYMEX prices were above spot contract prices held by the Trust, resulting in a realized loss on oil contracts of approximately \$2.6 million for the period. These fixed oil swap contracts were initially established to hedge approximately 50% of projected oil and natural gas liquids volumes. However, historically low natural gas prices, coupled with strong domestic natural gas liquids growth ahead of existing infrastructure, has resulted in reduced prices of natural gas liquids to well below their historical range of 45% to 50% of the price of WTI oil.

The Trust had forecasted 2012 first-quarter natural gas liquids to WTI of 49% and actual results for the quarter were 38%. This decoupling of natural gas liquids with WTI oil prices negatively impacted the Trust's financial results. Additionally, the Trust has no natural gas hedges in place.

Turning to drilling results in the Trust AMI, Chesapeake brought on line six gross wells in the three-month period from December through February of 2012 at varied networking interests. In addition, Chesapeake has drilled or participated in seven gross wells that were completed in March and April 2012. Including these second-quarter producing wells, Chesapeake has drilled or participated in approximately 26 of the 118 development wells.

It is required to drill or participate in prior to June 30, 2016, under the development agreement with Trust. Chesapeake is currently operating six rigs in the Trust AMI and plans to operate five to six rigs in the Trust AMI throughout 2012. This level of drilling is consistent with the drilling plans outlined in the Trust's prospectus.

We will now take any questions you may have. Operator, please open up the line for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Kevin Smith, Raymond James.

Kevin Smith - *Raymond James - Analyst*

Good morning, gentlemen. You said you had completed six rigs essentially for this quarter or six wells, sorry, for this quarter.

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

For this reporting quarter, yes, there were six gross wells.

Kevin Smith - *Raymond James - Analyst*

Got you. Is that a little bit lower your pace? I thought it was more like three wells per month.

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Well, you know, the calculation is a little bit different whether you are thinking about it on a gross or net basis, but --



Unidentified Company Representative

Yes, it's just going to always vary on time and completions, but it could be around, right, six to nine. We have seven already this current quarter that we are in.

Kevin Smith - *Raymond James - Analyst*

Got you. Okay, so this is just a little bit of a low quarter for completed wells versus kind of average, is that fair?

Unidentified Company Representative

Well, it's still kind of within the average range.

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Yes, the timing is -- can be a tad lumpy, but the biggest point here is that production is right in line or slightly ahead, and so that is really what matters. The timing of individual wells and when they come can be sometimes difficult on a specific 30-day period, but with production in line we feel like the timing of bringing on wells is in line, too.

Kevin Smith - *Raymond James - Analyst*

Fair enough. Are you guys seeing ethane rejection?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

No.

Kevin Smith - *Raymond James - Analyst*

No? Okay. And so are you seeing any sort of increases in NGL prices so far this quarter? Or are we still expecting to be kind of right below \$40 a barrel or right in that range?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

It has been a pretty tough quarter for NGL prices, as you know. A lot of research out there suggests that it's going to get better through the rest of the year and there has been some turnarounds. The number of things that have impacted the price that seemed to be short-term in nature; there is other views out there that say it could be tough all year. So we will remain optimistic on that front, but we will just have to see.

Kevin Smith - *Raymond James - Analyst*

Fair enough. Thank you.

Operator

(Operator Instructions) Aaron Terry, Kayne Anderson.

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Hi, gentlemen. Good morning. Just a few questions on NGLs, kind of following up on Kevin's questions. First off, where are your NGL barrels priced? Are you guys priced off of Conway or do you guys sell these priced off of Mont Belvieu?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Aaron, it depended a little bit on -- we have multiple marketing contracts out here. I don't have a breakdown in front of me.

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

But would it be fair to say you do have some Conway exposure?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Certainly.

Unidentified Company Representative

Yes.

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Then can you talk a little bit about -- I know that if you do have Conway exposure it seems like there is some solutions, like you were saying earlier, a lot of discussion about a lot of infrastructure projects coming online. Would you expect as those projects come online that you would see an improvement in pricing, or are there any specific projects we should watch just to understand how that will move the pricing?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

I don't have a list of specific projects for you, but they are all well talked about by our counterparts in the midstream part of the business. There is a lot of people out there trying to bring more NGL barrels to Mont Belvieu and close that gap, and there is a number of things underway that we are hopeful will be -- will get us there over time.

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Sure. And then what about the components of your NGL? Are you guys on the lighter side or are these heavier NGLs? Can you talk a little bit about how that mixture is?

Unidentified Company Representative

I don't have that here either. I know it varies across the field. No, sir, we don't have that.



Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Then I guess one last question then on the -- you said there was six gross wells completed. What was the net number of wells? You said that your interests vary across these. Do you have just a net number for the quarter?

Unidentified Company Representative

Well, there is two ways to look at net as we now normally do with the working interest and net revenue interest. But then the net wells for the trust, I believe, were calculated back to the theoretical working interest when we started.

And so that net is 8.6 as it's counting towards the Trust wells. (multiple speakers) It's actually greater because -- so these six wells actually had an average working interest higher than would have been forecast for the quarter.

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Right.

Unidentified Company Representative

So even though it was fewer gross wells kind of than peer average, the net was actually higher on that well set.

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Okay, that makes sense. One final question, I guess just following up one more time on the NGLs. Are your NGLs -- the contracts that are hedging those NGLs, are those tied to the oil or are you hedging now at the individual components?

Nick Dell'Osso - *Chesapeake Granite Wash Trust - EVP & CFO*

Our contracts are -- as we have disclosed in our original filing here, our contracts are all oil swap contracts used in proxy and our calculation of that obviously the percentage of WTI has moved. So that is (technical difficulty)

Aaron Terry - *Kayne Anderson Rudnick Investment Management - Analyst*

Okay, makes sense. Thanks, guys. There are no other questions.

Operator

(Operator Instructions) [Charles Springfield], private investor.

Charles Springfield - *Private Investor*

Gentlemen, can you explain or describe the effect that the confusion and headline news over your parent company, Chesapeake, the Aubrey McClendon, how that affects those of us who are owners in your trust and why we should believe that there aren't accounting things that have occurred at Chesapeake that could not be happening at Chesapeake Granite? It's the same, as I understand it, management structure. Thank you.

Nick Dell'Osso - Chesapeake Granite Wash Trust - EVP & CFO

Well, Charles, the Trust is a statutory trust, which has a specific set of assets in it, which we don't have any specific ability to influence or anything other than report on the production results of these wells. And so there is a pretty good distance there between the Trust and the parent company.

As to anything else that has been happening with the parent company, I think I will let our previous statements stand for themselves and I have to move on.

Operator

With no further questions in queue I would like to turn the conference back over for any additional or closing remarks.

Nick Dell'Osso - Chesapeake Granite Wash Trust - EVP & CFO

We would like to thank you for joining us for the call this morning. We look forward to visiting with you again after the second-quarter results.

Thank you. This concludes our call.

Operator

Again, that does conclude today's conference. Thank you for everyone's participation today.

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